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Supreme Court of the United States

October Term, 1976

No.

CHURCHILL FOREST INDUSTRIES (MANITOBA) LTD., CHURCHILL PULP MILL LTD., TECHNOPULP INCORPORATED, STEPHEN E. MOCHARY, JAMES M. BROWN, JR., CHESTER CHASTEK, RIVER SAWMILLS COMPANY and BLUE CONSTRUCTION CORPORATION,
Petitioners,

against

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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SECURITIES AND EXCHANGE COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Petitioners pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered in this action on January 14, 1977.

Opinions Below

The opinion of the Court of Appeals, which is not yet officially reported, is annexed as Appendix A. The two opinions of the United States District Court for the Dis-

trict of New Jersey (a) dismissing the original complaint (reported at 391 F. Supp. 1167), and (b) dismissing the amended complaint (unreported), are annexed as Appendices B and C respectively.

Jurisdiction

The judgment of the Court of Appeals was entered on January 14, 1977. This petition for a writ of certiorari was filed within 90 days of that date. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

Question Presented

Was the Third Circuit correct in holding—in conflict with decisions in other circuits and the reasoning in prior decisions of this Court—that federal securities law subject matter jurisdiction exists over an alleged fraud

(a) which, plaintiff concedes, had no domestic impact, either on American citizens or domestic securities markets, but rather

(b) was alleged to have been against only a foreign governmental entity which purchased abroad non-publicly traded debentures in exchange for money paid abroad to be used in developing a forestry complex in that foreign country,

merely on the basis that the occurrence of *any* activity in furtherance of the alleged fraud in the United States is sufficient to establish jurisdiction?

Statutes and Regulations Involved

Sections 17(a), 20(b) and 22 of the Securities Act of 1933, 15 U.S.C. §§77q(a), 77t(b) and 77v, and sections 10(b), 21(e) and (f), and 27 of the Securities Exchange Act of 1934, 15 U.S.C. §§78j(b), 78u(e) and (f), and 78aa, and Securities and Exchange Commission Rule 10b-5, 17 C.F.R. 240.10b-5, which are involved in this action, are set forth verbatim in Appendix D.

Statement of the Case

This action was commenced by the Securities and Exchange Commission ("SEC") on January 17, 1974 against Alexander Kasser* and petitioners ("defendants"), charging them with violating the anti-fraud provisions of the federal securities laws. The SEC sought an injunction against all defendants, restraining them from further violations of the securities laws, and an accounting and disgorgement by certain defendants of all amounts received by them as a result of the alleged fraud.

The fraud, as alleged in the amended complaint,** occurred in connection with the development of a forestry products complex at The Pas, Manitoba, Canada. The only party allegedly defrauded is specified to be the Manitoba Development Fund ("MDF"), a Crown corporation

* Kasser, who is the alleged principal wrongdoer, is not in the United States and the SEC has not effected service on him.

** The District Court found that the amended complaint "merely restates in more lengthy fashion the substance of the SEC's initial complaint" (A34). (References bearing the prefix "A" refer to the pages of the appendices to this petition.) Unless otherwise noted, only the allegations of the amended complaint will be discussed.

formed by the Province of Manitoba to promote industrial and regional development in that foreign province. The nature of the alleged fraud was identical in both counts of the amended complaint: the MDF was fraudulently induced to enter into investment contracts with two non-public companies which had agreed to develop parts of the complex, defendant Churchill Forest Industries (Manitoba) Ltd. ("CFI"), a privately-owned Manitoba corporation (Count I), and defendant River Sawmills Company ("River"), a privately-owned Delaware corporation (Count II). The investment contracts involved debentures of both CFI and River, acquired by MDF pursuant to a formula under which MDF purchased a certain amount of debentures for each dollar of equity capital invested in CFI and River. The alleged wrongdoing, in essence, involved misrepresentations concerning the amount of equity capital actually invested, the non-independent relationship of various of the parties involved in the development, and the use made of monies invested by the MDF.

The amended complaint made clear that the essence of this alleged fraud took place in Manitoba: the MDF, a Manitoba government corporation, was the only allegedly defrauded party, and it received the CFI and River debentures in Manitoba in exchange for funds paid by it in Manitoba. The SEC expressly conceded that the alleged fraud had no effect in the United States (A24 n.1).

There were three trust indentures and four written agreements relevant to the debentures purchased by the MDF. All three trust indentures were executed in Manitoba or Italy, and each contained a provision that it was to be construed in accordance with Manitoban law. The

amended complaint expressly alleged that three of the four agreements referred to therein were executed in Europe; no allegation was made as to the fourth except that it was "caused" to have been entered into in the United States. Three of these four agreements, including the latter one, expressly provided that they were to be construed in accordance with Manitoban law; a fourth agreement did not contain a choice-of-law provision, although it expressly provided that "where sums of money are mentioned in this Agreement, they shall always mean Canadian funds payable at par in the City of Winnipeg in the Province of Manitoba."

Notwithstanding the absence of effect in the United States, the consummation of the purchase and payment therefor in Canada, and the Manitoban choice-of-law provisions in controlling documents, the SEC sought to invoke United States jurisdiction on the basis of allegations of miscellaneous acts in the United States, including: negotiation of agreements; making of misrepresentations; use of United States mail; transmittal to the United States by defendants of proceeds they received in Canada; transmittal of funds from the United States to Canada; and the maintenance of books and records in the United States.

Defendants moved to dismiss for lack of subject matter jurisdiction; for the purposes of that motion, the factual allegations of the complaint were taken as true.

The original complaint was dismissed by the District Court for lack of subject matter jurisdiction on March 11, 1975, with leave granted to file an amended complaint. The court found that this action "involves essentially foreign transactions without impact in this country" and that "the

essentially foreign nature of the transactions here at issue is not materially altered by the various miscellaneous acts allegedly committed locally in furtherance of the scheme" (A32).

The SEC then filed its amended complaint, which was also dismissed by the District Court for lack of subject matter jurisdiction on November 17, 1975. The District Court stated that the denial of jurisdiction in this action was consistent with the recent decisions of the Court of Appeals for the Second Circuit in *IIT* v. *Vencap, Ltd.*, 519 F.2d 1001 (1975), and *Bersch* v. *Drexel Firestone, Inc.*, 519 F.2d 974, *cert. denied sub nom. Bersch* v. *Arthur Andersen & Co.*, 423 U.S. 1018 (1975).

On January 14, 1977, the Court of Appeals for the Third Circuit reversed the decision of the District Court. The Court of Appeals, while noting the lack of impact of the alleged fraud on American investors or domestic securities markets, sustained jurisdiction on the ground that "the federal securities laws do grant jurisdiction in transnational securities cases where at least some activity designed to further a fraudulent scheme occurs within this country" (A9).

Reasons for Granting the Writ

As hereinafter discussed, each of the following bases warrants granting this petition: conflict among the circuits; conflict with relevant decisions of this Court; and, to the extent it is held that no prior decision of this Court has decided the issue, this petition presents an important question of law not yet determined by this Court.

A. Conflict Among the Circuits

In holding here that "the federal securities laws do grant jurisdiction in transnational securities cases where at least some activity designed to further a fraudulent scheme occurs within this country" (A9), even though the alleged fraud was addressed only to a foreign governmental entity, was consummated outside the United States and was concededly without impact on American investors or American securities markets, the Third Circuit conflicts with prior decisions of *every* circuit court—the Second, Eighth and Ninth—and numerous district courts which have decided this issue.

1. Second Circuit Decisions

The Second Circuit's most recent decisions on this issue were in two opinions, issued on the same day, in *Bersch* v. *Drexel Firestone, Inc.*, 519 F.2d 974 (2d Cir.), *cert. denied sub nom. Bersch* v. *Arthur Andersen & Co.*, 423 U.S. 1018 (1975), and *IIT* v. *Vencap, Ltd.*, 519 F.2d 1001 (2d Cir. 1975).

The Second Circuit's decisions in *Bersch* and *IIT* conflict with the Third Circuit's here, since the Second Circuit rejected the concept—on which the Third Circuit relied here—that subject matter jurisdiction exists over sales of securities to foreigners abroad, whenever, to quote the Third Circuit's opinion, "at least some activity designed to further a fraudulent scheme occurs within this country." Significantly, although the Second Circuit rejected the view subsequently adopted by the Third Circuit here, the Second Circuit recognized that even its decisions went beyond prior holdings on the subject. Thus, the Second Circuit in these

opinions expressly stated that (a) prior decisions required proof of impact on domestic investors or securities markets in order to sustain jurisdiction (*Bersch*, 519 F.2d at 987 n.29); (b) both *Bersch* and *IIT* claim to "extend . . . the application of the securities laws to transnational transactions beyond prior decisions" (*IIT*, 519 F.2d at 1018; *see also Bersch*, 519 F.2d at 987); (c) the court was "unable" to "point to language in the statutes, or even in the legislative history, that compelled" the court's extension of jurisdiction (*Bersch*, 519 F.2d at 993); (d) "reasonable men might conclude that [jurisdictional] coverage" was less than was outlined in the two opinions (*Bersch*, 519 F.2d at 993); and (e) *IIT* was "*sui generis*" (*IIT*, 519 F.2d at 1019).

Analysis of the facts in *Bersch* demonstrates its conflict with the Third Circuit here. The *Bersch* court noted the existence of numerous acts committed within the United States, of a nature substantially similar to those alleged in the amended complaint here: meetings "in New York on numerous occasions to initiate, organize and structure" the fraudulent offering; retention of a New York law firm which "had numerous meetings"; retention of New York accountants; drafting and delivery of drafts of the fraudulent representations in New York; and "accounts for the proceeds of the" fraud "were opened at the Bank of New York and the proceeds in dollars were to be deposited there" (519 F.2d at 985 n.24). The *Bersch* court even assumed "there was some mailing . . . into the United States" of the fraudulent misrepresentations "and some reliance on them" (*Id.* at 991).

Despite these numerous acts within the United States, the Second Circuit in *Bersch* denied subject matter jurisdiction in so far as the fraud involved "sales of securities to foreigners outside the United States" (519 F.2d at 993). It did so by establishing three tests for subject matter jurisdiction dependent on the citizenship and situs of the allegedly defrauded party: (1) federal jurisdiction exists over "sales of securities to Americans resident in the United States whether or not acts . . . of material importance occurred in this country"; (2) federal jurisdiction exists over losses from "sales of securities to Americans resident abroad if, but only if, acts . . . of material importance in the United States have significantly contributed thereto"; and (3) federal jurisdiction does not exist over losses from "sales of securities to foreigners outside the United States unless acts . . . within the United States directly caused such losses." *Id.* at 993. Viewed against that third test for sales of securities to foreigners abroad (the only test relevant here), the Second Circuit found the various miscellaneous acts within the United States—even more significant than those present here—did not "directly cause" the losses, and thus were insufficient to sustain jurisdiction. The Second Circuit therefore reversed the lower court's decision that there was jurisdiction as to such plantiffs.*

* *Bersch* involved an offering of stock in a Canadian corporation, via American and foreign brokers, to Americans and foreigners living abroad and, apparently, Americans residing in the United States. The Second Circuit held that the various acts within the United States were sufficient to sustain jurisdiction over sales to Americans both in the United States and abroad, but insufficient on sales to foreigners abroad—*i.e.*, these acts within the United States were of "material importance" that "significantly contributed" to the losses (the test on sales to Americans abroad), although they did not "directly cause" the losses (the test on sales to foreigners abroad). Here, while finding it unnecessary to decide the issue, in view of its very broad holding on jurisdiction, the Third Circuit questioned "whether it can be convincingly maintained that [miscellaneous] acts within the United States did not directly cause any extraterritorial losses" (A12).

Significantly, the Second Circuit quoted with approval the following portion of *Investment Properties International, Ltd.* v. *I.O.S., Ltd.,* [1970-71] CCH Fed. Sec. L. Rep. ¶93,011 (S.D.N.Y. 1971), *aff'd on expedited appeal without opinion* (Docket No. 71-593, 2d Cir. 1971)—which is directly contrary to the Third Circuit's opinion here:

> "If there is no such domestic impact from a substantially foreign transaction, United States courts have no reason to become involved, and compelling reason *not* to become involved, in the burdens of enforcement and the delicate problems of foreign relations and international economic policy that extraterritorial application may entail." *Id.* at p. 90,735 (emphasis in original).

The *IIT* decision, issued by the same Second Circuit panel simultaneously with the *Bersch* decision, must be presumed to be consistent with *Bersch*. While *IIT* is less elucidating of the Second Circuit position, both because the Second Circuit described that case as *"sui generis"* and found the record incomplete, thus requiring a remand to fill that void, that opinion, too, contains language in conflict with the Third Circuit's holding here. Thus, the *IIT* opinion states that subject matter jurisdiction is not created merely because preparatory acts occurred in the United States (519 F.2d at 1018). Further, the *IIT* opinion emphasized that *"the securities laws are not to apply in every instance where something has happened in the United States"*; rather, the determination must take into account how "large the gap between the something and a consummated fraud" and how "negligible the effect in the United States or on its citizens." *Ibid.* (emphasis added). And the

IIT opinion expressly labels as "weak with respect to subject matter jurisdiction," an alleged fraud against "a highly sophisticated [foreign] investor, advised by experienced counsel . . . [who] had participated to some extent in the drafting" of the agreements (*id.* at 1011-12)—exactly what is alleged here and yet held sufficient for jurisdiction by the Third Circuit.

Both prior Second Circuit decisions and subsequent decisions by district courts in that circuit support the conclusion that the Second Circuit's view conflicts with the Third Circuit's holding that jurisdiction exists over "transactional securities cases where at least some activity designed to further a fraudulent scheme occurs within this country."

For example, in *Leasco Data Processing Equipment Corp.* v. *Maxwell,* 468 F.2d 1326 (2d Cir. 1972), the Second Circuit indicated that "some activity" within the United States is insufficient to support jurisdiction, by stating that jurisdiction would not exist if foreign businessmen "met in New York for convenience and" one foreign businessman "fraudulently induced the [other] to make purchases of [foreign] securities" in other countries. *Id.* at 1338. Further, the Second Circuit explained there that jurisdiction over a sale of securities consummated abroad could not be based solely on domestic activities involving misrepresentations in the United States, meetings in, telephone calls to and from, and mailings to and from the United States, and the execution of the contract of sale in the United States. Rather, jurisdiction was upheld there only

because such activities within the United States were combined with impact on domestic investors.*

A Second Circuit district court opinion following *Bersch* and *IIT* demonstrates a continued rejection of the view that "some activity" in the United States is sufficient for jurisdiction. Thus, in *F.O.F. Proprietary Funds Ltd.* v. *Arthur Young & Co.*, 400 F.Supp. 1219 (S.D.N.Y. 1975), the court, relying on *Bersch* and *IIT*, denied subject matter jurisdiction over an alleged securities fraud, despite substantial conduct in the United States, including drafting of the misrepresentations, making of the decision to sell the securities, making of decisions as to use of proceeds of the alleged fraud, and sales activities. The court recognized that the activity in the United States would permit the conclusion that the defendants "operating from the United States, allegedly devised and carried out a scheme to sell debentures issued and guaranteed by American companies." *Id.* at 1222. Yet, looking to the essentials of the transaction, the

* Other decisions by the district courts in the Second Circuit, prior to *Bersch* and *IIT*, rejected the "some activity" test on which the Third Circuit decision here rests. For example, in *Kook* v. *Crang*, 182 F.Supp. 388, 390 (S.D.N.Y. 1960), the court denied jurisdiction despite use of United States mail and telephone, and other domestic activity, since the "essentials of [the] transactions"—the place where the binding commitment was made and where the exchange of securities for money occurred—were in Canada. *Accord, Sinva, Inc.* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 48 F.R.D. 385 (S.D.N.Y. 1969) (jurisdiction denied since essentially foreign transaction despite defendant's arranging for and obtaining payment in New York; see prior opinion at 253 F.Supp. 359, 367); *Selzer* v. *The Bank of Bermuda, Ltd.* [1974-75] CCH Fed. Sec. L. Rep. ¶94,876 at p. 96,996 (S.D.N.Y. 1974) (extraterritorial jurisdiction requires both "some significant connection in the violations with the United States" and that "the effects of the violations are detrimental to American investors"); *Manus* v. *The Bank of Bermuda, Ltd.*, [1971-72] CCH Fed. Sec. L. Rep. ¶93,299 (S.D.N.Y. 1971); *Finch* v. *Marathon Securities Corp.*, 316 F.Supp. 1345 (S.D.N.Y. 1970); *Investment Properties Int'l, Ltd.* v. *I.O.S., Ltd., supra.*

court dismissed the complaint for lack of jurisdiction since the debentures, which were the subject of the alleged fraud, "were offered only to purchasers outside the United States ... and were issued to raise capital for foreign investment." *Id.* at 1223. The controlling fact was that the conduct directly causing the loss—the sale of the debentures, based on information communicated to the purchasers—occurred outside the country; all other acts of "operating" from, and "devis[ing] and carr[ying] out [the] scheme" in, the United States, were held to be " 'mere preparation' of the fraud" which, the court held, under *IIT*, cannot sustain subject matter jurisdiction. *Id.* at 1222-23. The Third Circuit here, on substantially identical facts—an alleged fraud, only part of which was allegedly devised in and carried out from the United States, involving the sale of debentures abroad to a foreign entity in order to raise capital for foreign investment—reached a diametrically opposite result, indicating the clear conflict between the two circuits.*

2. *Eighth Circuit Decision*

The Eighth Circuit, in *Travis* v. *Anthes Imperial Ltd.*, 473 F.2d 515 (8th Cir. 1973), indicated that "some activity" in the United States was not sufficient to create subject matter jurisdiction; rather, it held, both domestic impact and "significant conduct" (*id.* at 524) in the United States

* The Third Circuit recognized that its decision here was not consistent with the holdings in *IIT* and *Bersch*. While calling *IIT* "more supportive of subject-matter jurisdiction here" (A8), it noted that *IIT* expressly denied that jurisdiction would exist merely because some activity occurred in the United States, where that activity was "mere preparatory activit[y]" as distinguished from the "perpetration of fraudulent acts themselves" (A10). And as to *Bersch*, the Third Circuit conceded *Bersch* was contrary in denying jurisdiction where the purchasers were foreigners living abroad (A11-12).

were required. The *Travis* court found domestic impact due to the "substantial" effect on the value of the stock held by Americans resident in the United States. *Id.* at 528. In sustaining jurisdiction, it quoted with approval from the Second Circuit decision in *Leasco,* that "the scales are tipped in favor of" subject matter jurisdiction "because misrepresentations were made in the United States." *Id.* at 526. Obviously, such "tipp[ing] in favor of jurisdiction" involves the combination of two factors—domestic impact and domestic conduct—neither one by itself being sufficient for jurisdiction. For if the misrepresentations within the United States were sufficient by themselves to sustain jurisdiction, the *Travis* court would not have been required to discuss the domestic impact, and the opinion could have been limited to a one-sentence reference to the domestic conduct. Indeed, the *Travis* court's holding that "some activity" within the United States is not sufficient is made clear in its statement that jurisdiction would *not* have existed in that case if, instead of the consummation—the purchase of stock in a Canadian corporation—having occurred in the United States, the "American citizens [had] gone to Canada and purchased [the] stock." *Id.* at 528.

3. *Ninth Circuit Decisions*

In an enforcement action brought by the SEC against a Delaware corporation, the Ninth Circuit refused to rely solely on admitted use of interstate commerce facilities to sustain jurisdiction, preferring instead to "focus . . . upon [defendants'] activities within the United States *and* the impact of those activities upon American investors." *Securities and Exchange Commission* v. *United Financial*

Group, Inc., 474 F.2d 354, 356-57 (9th Cir. 1973) (emphasis added).*

The Ninth Circuit's view that extraterritorial jurisdiction over an essentially foreign fraud exists only if a domestic impact is shown was reiterated in a decision rendered only ten days after the Third Circuit's decision here. *Des Brisay* v. *The Goldfield Corp.* [Current] CCH Fed. Sec. L. Rep. ¶95,868 (9th Cir. 1977). Although some activity in furtherance of the alleged fraud occurred in the United States, the Ninth Circuit ignored such conduct as a basis for jurisdiction, relying instead on the fact that the fraud had "an adverse impact on domestic securities markets" since the stock involved was listed on the American Stock Exchange (*id.* at p. 91,193). Significantly, the Ninth Circuit felt compelled to distinguish *Bersch* v. *Drexel Firestone, Inc., supra,* where jurisdiction was not upheld over a fraud in so far as it involved sales of securities to foreigners outside of the United States, on the ground that, since the stock in *Bersch* was not "listed on an American securities exchange," there was no domestic impact (*id.* at p. 91,194 n.4). Application of the Ninth Circuit reasoning in *Des Brisay* to the instant facts, where the absence of domestic impact is conceded by the SEC, would result in a finding that no jurisdiction exists here—directly contrary to the Third Circuit's holding.

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* The SEC had urged that the mere use of the facilities of interstate commerce would sustain jurisdiction. The Ninth Circuit found it unnecessary to decide that contention, preferring instead to rest its decision on the combination of domestic activity *and* domestic impact.

4. Other District Court Decisions

While no other circuit court has considered this issue, decisions of other district courts heighten the need for this Court to determine the conflict of holdings caused by the Third Circuit in this action.

In *Securities and Exchange Commission* v. *Gulf Intercontinental Finance Corp.*, 223 F.Supp. 987 (S.D. Fla. 1963), the court did not base jurisdiction on the use of United States mails, but upheld jurisdiction over a mainly Canadian sale of securities by a Canadian corporation organized by United States citizens, due to finding domestic impact of misrepresentations to American citizens in the United States. *Id.* at 994, 995.

For other district court opinions in conflict with the Third Circuit's decision here, see *Securities and Exchange Commission* v. *Capital Growth Co., S.A.* (*Costa Rica*), 391 F. Supp. 593, 597 (S.D.N.Y. 1974) (jurisdiction exists if there was "significant conduct" in the United States or "extraterritorial conduct which was harmful to and which had an impact upon United States investors"); *Garner* v. *Pearson*, [1973-74] CCH Fed. Sec. L. Rep. ¶94,549 at p. 95,906 (M.D. Fla. 1974) (jurisdiction found because fraud had a "significant impact on American investors"); *Selas of America (Nederland) N.V.* v. *Selas Sorp. of America*, 365 F.Supp. 1382, 1386 (E.D.Pa. 1973) (jurisdiction upheld where "sufficient conduct took place within the U.S." and the transaction had "significant impact on American securities markets"); *United States* v. *Clark*, 359 F.Supp. 131 (S.D.N.Y. 1973) (jurisdiction upheld because of "substantial detrimental effects on the interests of American investors"). See also the cases cited at pp. 12-13 *supra*.

Significantly, prior to the Third Circuit's decision in this action, but after the Second Circuit's opinions in *IIT* and *Bersch*, another district court within the Third Circuit dismissed a securities fraud complaint for lack of subject matter jurisdiction despite activity within the United States, including defendants' obtaining payments in the United States, and plaintiffs' accompanying defendants' salesmen to the United States to make withdrawals from a United States bank to pay for an additional purchase. *Recaman* v. *Barish*, 408 F.Supp. 1189 (E.D. Pa. 1975).

5. Summary

The Third Circuit decision here is in conflict with every prior decision of other circuits and with numerous prior decisions of district courts. This conflict, created by the decision below, should be resolved by this Court.*

B. Conflict With Decisions of This Court

While the present issue has not been expressly posed to this Court, prior decisions of this Court, both in a recent decision in which this issue was implicitly decided and in

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* Interestingly, the Third Circuit itself, as recently as 1975, stated that a "long series of Supreme Court cases has held that before a jurisdiction can seek extraterritorial application of its laws, it must have a substantial interest in the party whom the statute seeks to protect. . . . Where no such overwhelming interest in the parties is present, however, the Supreme Court has refused to allow the extraterritorial application of a local statute. In Lauritzen v. Larsen, 345 U. S. 571 . . . (1952), the Supreme Court overturned a trial court's application of the Jones Act to a Danish seaman injured in Cuban waters who had signed an employment contract in an American port. *Accord*, Home Ins. Co. v. Dick, 281 U.S. 397 . . . (1929)." *Henry* v. *Richardson-Merrell, Inc.*, 508 F.2d 28, 39 n.25 (3d Cir. 1975).

decisions on extraterritorial jurisdiction of other statutes, conflict with the Third Circuit's decision in this action.

The issue of the extraterritorial jurisdiction of the securities acts, while not expressly posed, implicitly had to have been decided by this Court in *Scherk* v. *Alberto-Culver Co.*, 417 U.S. 506 (1974), where the defendant, relying on a pre-dispute arbitration agreement, had sought to stay a securities fraud action pending arbitration. Previously, in *Wilko* v. *Swan*, 346 U.S. 427 (1953), this Court had held that a lawsuit within federal securities acts jurisdiction may not be stayed for arbitration. Hence, a determination whether federal securities acts jurisdiction existed over the transaction alleged in *Scherk* was crucial to the motion to stay the court action pending arbitration.*

This Court recognized that the transactions in *Scherk* involved substantial activity within the United States, including the conducting of negotiations in the United States (*id.* at 508) and the making of "fraudulent representations and omissions . . . within the jurisdiction of the United States" (*id.* at 522; dissent). However, looking to the essentially foreign nature of the transaction, "a truly international agreement," the subject matter of which concerned investments "primarily situated in European countries" (*id.* at 515), with an impact on foreign business, not

* The district court in *Scherk* had held that securities acts jurisdiction existed on the dispute and thus stayed the arbitration, relying on *Wilko* v. *Swan*, and denied a motion to dismiss for lack of subject matter jurisdiction. While the arbitration stay was immediately appealable, the denial of the motion to dismiss obviously was not, and therefore the "contention" that "the complaint be dismissed because the federal securities laws do not apply to this international transaction, cf. *Leasco Data Processing Equipment Corp.* v. *Maxwell*, 468 F.2d 1326 (CA2 1972) . . . [was] not before this Court." *Scherk* v. *Alberto-Culver Co.*, 417 U.S. at 516 n.9.

domestic securities markets, this Court refused to stay arbitration, thus implicitly finding that there was no subject matter jurisdiction. To paraphrase this Court's recitation of the criteria in *Scherk, id.* at 515, here too:

> the negotiations leading to the signing of the contract . . . took place in the United States, Switzerland and Italy, among other countries. . . . Most significantly, the subject matter of the contracts concerned a Canadian provincial government entity's purchase of debentures to finance the development of a forestry complex situated in Canada.

Yet, despite these almost identical facts, the Third Circuit held here that the securities acts were applicable, while this Court in *Scherk* implicitly decided to the contrary.

Interestingly, the dissent in *Scherk*, which believed that the arbitration should have been stayed because the dispute was within securities acts jurisdiction, recognized that some conduct within the United States, by itself, could not sustain §10(b) jurisdiction. Thus, the dissent stated that "[f]ederal jurisdiction under the 1934 Act will attach only to *some* international transactions." *Id.* at 534 (emphasis added). The elements noted by the dissent which, *when added to conduct within the United States,* would establish §10(b) jurisdiction are "defrauded American investors" (*id.* at 529) and "economic impact of the alleged fraud . . . within the United States" (*id.* at 529-30 n.8)—neither of which exists here.

In opinions on the analogous issue of extraterritorial jurisdiction of other federal statutes, this Court has held that "some conduct" within the United States is insufficient to sustain jurisdiction in the absence of domestic impact.

In *Foley Bros., Inc.* v. *Filardo,* 336 U.S. 281 (1949), this Court, before considering the extraterritorial jurisdiction of the specific federal statute there involved, made the general observation, applicable to all federal legislation, that all federal statutes were to be construed "to apply only within the territorial jurisdiction of the United States, . . . based on the assumption that Congress is primarily concerned with domestic conditions." *Id.* at 285. Then, this Court turned to the specific issue there involved: the applicability of the eight-hour law to the employment of an American citizen by an American contractor on a foreign construction project. There was no dispute that the plaintiff American citizen employee had contracted in the United States for such employment before traveling from the United States to the foreign construction project, and that the relevant written document had been executed in the United States. Yet, since performance was to be abroad, this Court held that it was an essentially foreign transaction over which no subject matter jurisdiction existed.

This Court relied on impact within the United States —not just conduct within the United States—in upholding subject matter jurisdiction of the antitrust laws over multinational transactions. In *United States* v. *Sisal Sales Corp.,* 274 U.S. 268 (1927), the defendants, Mexican and American corporations, were charged with restraining the importation of sisal from Mexico to this country. The conspiracy was entered into in the United States and acts in furtherance of the conspiracy took place in the United States and Mexico. Jurisdiction was upheld because acts took place in this country which "brought about forbidden

results within the United States." *Id.* at 276. See also *Thomsen* v. *Cayser,* 243 U.S. 66 (1917).

In *Lauritzen* v. *Larsen,* 345 U.S. 571 (1953), this Court refused to extend the application of the Jones Act to a foreign seaman injured on a foreign ship in foreign waters, even though the employment contract had been signed in the United States. *Cf. New York Central R. Co.* v. *Chisholm,* 268 U.S. 29 (1925) (this Court refused to apply the Federal Employers' Liability Act extraterritorially where an American employee of an American railroad was killed in Canada on board a New York-Montreal train).

In *McCulloch* v. *Sociedad Nacional de Marineros de Honduras,* 372 U.S. 10 (1963), this Court held that the National Labor Relations Act did not apply extraterritorially. In that case, an American union sought to invoke provisions of the Act against a foreign ship, owned by a foreign subsidiary of an American company, manned by foreign seamen represented by a foreign union; the ship travelled regularly between Central American and United States ports. While noting that Congress could have constitutionally extended the Act to foreign ships while in American waters, this Court held that Congress intended the Act to protect American workers only and was inapplicable to foreign workers. *See also Benz* v. *Compania Naviera Hidalgo, S.A.,* 353 U.S. 138 (1957), for the same result concerning the Labor Management Relations Act.

These prior decisions of this Court required something more than "some" conduct within the United States to sustain subject matter jurisdiction—they required domestic impact as well.* Indeed, as quoted *supra,* p. 17n., the Third

* This Court has mandated the same prerequisite to the extraterritorial application by a state of its statutes to multi-state activity. *See, e.g., Strassheim* v. *Daily,* 221 U.S. 280 (1911); *Watson* v. *Employers Liability Assurance Corporation, Ltd.,* 348 U.S. 66 (1954).

Circuit itself recognized that a "long series of Supreme Court cases has held" that extraterritorial jurisdiction does not exist unless the jurisdiction seeking such extraterritorial application of the law in question has "a substantial interest in the party whom the statute seeks to protect." *Henry* v. *Richardson-Merrell, Inc., supra,* 508 F.2d at 39 n.25. Yet, by upholding jurisdiction here, on the basis of "some activity" within the United States, over a transaction without any domestic impact, the Third Circuit has ignored and decided contrary to the "long series of Supreme Court cases" referred to in *Henry* and which are discussed above.

C. Important Question Not Yet Decided by This Court

We believe, as discussed in the preceding portion of this petition, that this Court has implicitly decided the issue here involved, contrary to the Third Circuit's decision in this action. If this Court believes that its prior decisions did not definitively decide the issue of the extraterritorial jurisdiction of the federal securities acts, we believe this important question should now be decided by this Court.

This issue is one that is arising with increasing frequency in our courts. In part, this is due to what this Court has recognized to be the increasingly international character of the American economy:

> "For at least two decades we have witnessed an expansion of overseas commercial activities by business enterprises based in the United States. The barrier of distance that once tended to confine a business concern to a modest territory no longer does so." *The Bremen* v. *Zapata Off-Shore Co.,* 407 U.S. 1, 8 (1972).

With this increase in international transactions by Americans has come an increase in allegations of wrongdoing,

including securities frauds, by Americans. Since the first reported decision on the extraterritorial scope of the federal securities laws in 1960, *Kook* v. *Crang, supra,* the number of such decisions has markedly increased, almost in geometric proportions.

The Director of the SEC's Enforcement Division has been quoted as saying that the Third Circuit's decision here is " 'extremely important' for the agency and would help it pursue 'a number of other cases' where foreign investors allegedly were defrauded by U.S. citizens." *Wall Street Journal,* January 21, 1977, at 4, col. 3.

The question "whether Congress would have wished the precious resources of United States courts and law enforcement agencies to be devoted to" protecting foreign investors in cases where there is no impact on the United States (*Bersch* v. *Drexel Firestone, Inc., supra,* 519 F.2d at 985) is an important question which should be decided by this Court at this time.*

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* This issue is ripe for decision now, despite the fact that it arises on a motion to dismiss and the case has been remanded for pre-trial proceedings and a trial. No factual findings are required since, for purposes of the motion to dismiss, no dispute exists on the relevant facts: the identity of the sole injured party, the MDF; the consummation of the allegedly fraudulent transactions abroad; the foreign purpose for which the proceeds were to be used; the contents of relevant documents; and the activity involved within the United States. During oral argument before the Third Circuit, counsel for both parties expressly stated, in response to a question from the court, that a remand to obtain additional facts would add no material facts and that, therefore, the issue was ripe for decision on the present record. If the Third Circuit's ruling remains undisturbed, a full trial would be required; if the decisions of the other circuits and the reasoning of prior decisions of this Court were held controlling, dismissal of the complaint here without the time and expense of a trial would be required. Hence, if petitioners are correct in their position that no subject matter jurisdiction exists, they would be severely prejudiced by being required to expend substantial amounts of time and money in preparing for and defending in a trial on the merits, when that could be avoided by an immediate decision by this Court.

Conclusion

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDICES

APPENDIX A

Opinion of the Court of Appeals, January 14, 1977

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 76-1332

Securities and Exchange Commission,
Appellant,

v.

Alexander Kasser, Stephen E. Mochary, Technopulp Incorporated, Churchill Forest Industries (Manitoba) Ltd., Churchill Pulp Mill Ltd., James M. Brown, Jr., Chester Chastek, River Sawmills Company & Blue Construction Corporation, (Defts. in D. C.) Betram Verkaufs-AG, (Addl. Deft. on cross claim in D. C.)

On Appeal from the United States District Court
for the District of New Jersey (Newark)
Civil Action No. 74-90
Argued November 8, 1976

Before: ADAMS and WEIS, *Circuit Judges,* and
FOGEL, *District Judge**

OPINION OF THE COURT

(Filed Jan 14 1977)

* Sitting by designation.

Appendix A

ADAMS, *Circuit Judge.*

The central issue in this case is whether the Securities and Exchange Commission (SEC) may invoke the jurisdiction of the federal courts over defendants who have allegedly engaged in fraudulent conduct within the United States, when the sole victim is a foreign corporation and when the purported fraud had little, if any, impact within this country.

I.

For the purpose of this appeal, the allegations of the amended complaint are deemed to be true and will serve as the factual base with which to resolve the jurisdictional issues raised here.[1] Inasmuch as the district court aptly summarized the facts proffered by the pleadings, we need not narrate them at length.[2] Rather, we shall outline only those facts that are necessary for our decision.

Basically, the SEC avers that the defendants engaged in a scheme to defraud and make misrepresentations to the Manitoba Development Fund ("Fund") with respect to the purchase and sale of various securities, including investment contracts, debentures and stock, both preferred and common. The Fund, the sole victim of the fradulent conduct, is a corporation wholly owned by the Province of Manitoba, Canada. It was formed to interest private enterprise in the creation of a forestry development in that province.

1. *See* Lasher v. Shafer, 460 F.2d 343, 344 (3d Cir. 1972); Sabolsky v. Budzanoski, 457 F.2d 1245, 1249 (3d Cir.), *cert. denied*, 409 U.S. 853 (1972).

2. The opinion of the district court is reported at 391 F. Supp. 1167 (D.N.J. 1975). That opinion was written in connection with the dismissal of the original complaint. The amended complaint, filed by leave of the district court, also was dismissed in an opinion that is unreported. For the text of the unreported opinion, see Appendix at 264-70. The basis for the dismissals of both complaints is exactly the same—to wit, a lack of subject-matter jurisdiction over the securities fraud alleged to have been devised by the defendants.

Appendix A

According to the SEC, Kasser and his co-defendants induced the Fund to enter into investment contracts with and acquire debentures of two defendant corporations, Churchill Forest Industries ("CFI") and River Sawmills Company ("River"). These two corporations as well as several others involved in the allegedly fraudulent dealings were largely owned and dominated by Kasser. While CFI was a Canadian corporation with offices in Montclair, New Jersey, River was a Delaware corporation with offices at the same location. Apparently, the Fund entered into the contracts and acquired the debentures based on false representations that Kasser and his associates, or corporations that they controlled, had invested and would invest capital in equity securities of CFI and River over and above the proceeds obtained from debenture sales to the Fund.

Under the investment contracts, the Fund was to make loans to CFI and River in exchange for the debentures. Each loan disbursement would be granted only upon certification that the defendants or their controlled corporations had effected the required equity investments. Both the loans and the equity proceeds were to be spent to establish the forestry development. However, the defendants never made, nor did they intend to make, the equity investments. Instead, they recirculated the proceeds of the loans and debenture transactions in a "ponzi"-like scheme: the defendants made the purported equity investment not with additional capital but with the very money previously made available by the Fund.

The fraud was implemented, in part, by "laundering" the Fund's loan disbursements through various corporations and bank accounts in the United States, Canada, and Switzerland. Over several years, the Fund invested roughly $45,000,000 in debt securities issued by CFI and River, and these payments were made, it is asserted, because of continuous misrepresentations to and concealment of mate-

rial facts from the Fund. The defendants falsely represented that substantial equity capital had been invested in CFI and River and spent for development of the forestry complex. Moreover, they diverted much of the money invested in CFI and River to their own personal use. As a result, CFI and River have become bankrupt.

Transnational in character, the fraudulent transactions arranged by the defendants spanned at least two continents. But it is clear that a number of acts were committed within the United States. In its opinion, the district court expressly noted that the following conduct had occurred in this country: (1) various negotiations; (2) execution of one of the investment contracts in New York; (3) utilization of the instrumentalities of interstate commerce (*e.g.*, telephones and mails) to further the scheme; (4) incorporation of defendant companies in the United States, or at least the establishment of corporate offices; and (5) use of the New York office of a Swiss bank as a conduit for moneys received from the Fund.[3] Other activities taking place within the United States, according to the complaint but not mentioned by the district court, include (1) the maintenance of books and records in this country;[4] (2) drafting of agreements executed elsewhere;[5] and (3) transmittal of proceeds from the transactions to and from the United States.[6] In short, there was significant conduct which formed part of the defendants' scheme that did occur within this country.

By contrast, it is questionable whether any effect in the United States was wrought by the alleged fraudulent activities of the defendants. The SEC really does not claim that there was any such effect. Apparently, none of the

3. 391 F. Supp. at 1176.

4. *See* Amended Complaint at 7, 23-25 (Appendix at 129, 145-48).

5. *See, e.g.*, Amended Complaint at 9-15 (Appendix at 131-37).

6. *See, e.g.*, Amended Complaint at 19-20 (Appendix at 141-42).

securities was traded on any American exchange, nor did such sales have any measurable impact on domestic markets. In addition, no sale was made to any resident or citizen of this country, the sole victim of the defendants being the Fund, a Canadian corporation.

The SEC brought this action in the New Jersey district court, alleging that the defendants, individual and corporate, violated various antifraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934.[7] It sought injunctions against any further violations as well as ancillary relief. However, the district court dismissed the complaint with prejudice, holding that it lacked subject-matter jurisdiction over the alleged fraud. The SEC then filed the present appeal in this Court.

Since we believe that a district court does have jurisdiction in an SEC suit for injunctive relief under the federal securities laws, given circumstances such as are presented here, we reverse and remand.

II.

In dismissing the SEC's complaint for injunctive relief, the district court concluded that it lacked subject-matter jurisdiction over the alleged fraudulent activities. That court bottomed dismissal on the ground that the claimed fraud entailed "essentially foreign transactions without impact in this country."[8] The district judge reasoned that

7. The SEC contends that the defendants violated §17(a) of the Securities Act of 1933, 15 U.S.C. §77q(a); §10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b); and Rule 10b-5, 17 CFR 240.10b-5, the latter having been promulgated by the SEC pursuant to §10b of the 1934 Act.

The SEC brought its action under the jurisdictional provisions of the 1933 and 1934 Acts governing injunctions: §20(b) of the Securities Act of 1933, 15 U.S.C. §77t(b) and §21 of the Securities Exchange Act, 15 U.S.C. §78u.

8. 391 F. Supp. at 1177.

conduct without such effect is insufficient for jurisdiction to attach. Even though this premise constituted the essence of its decision to dismiss, the court assumed that conduct without effect in the United States could give rise to jurisdiction. But the trial judge stated that the intranational conduct of the defendants here consisted merely of "miscellaneous acts,"[9] not substantial enough to alter the foreign nature of the transaction. In their briefs and at oral argument, defendants in large part adopted the analysis of the district judge.

Although this case presents a relatively new legal problem, several opinions already have addressed similar matters.[10] They, and their underlying principles, suggest that the district court's position is too restrictive and that jurisdiction should vest.

Just recently, this Court in *Straub* v. *Vaisman & Co.*,[11] considered the jurisdictional aspects of transnational securities fraud. There, an American broker-dealer engaged in fraudulent sales of securities to nonresident foreigners. A unanimous panel of this Court found jurisdiction under the 1933 and 1934 Acts. Speaking for the panel, Judge Weis posited that "[c]onduct within the United States is alone

9. *Id.* at 1176.

10. Straub v. Vaisman & Co., 540 F.2d 591 (3d Cir. 1976); IIT v. Vencap, Ltd., 519 F.2d 1001 (2d Cir. 1975); Bersch v. Drexel Firestone, Inc., 519 F.2d 974 (2d Cir.), *cert. denied sub nom.* Bersch v. Arthur Andersen & Co., 423 U.S. 1018 (1975), Leasco Data Processing Equipment Corp. v. Maxwell, 468 F.2d 1326 (2d Cir. 1972). *See also* Travis v. Anthes Imperial, Ltd., 473 F.2d 515 (8th Cir. 1973).

For commentary discussing some of these cases, see *e.g.*, Note, *Extraterritorial Application of §10(b) of the Securities Exchange Act of 1934—The Implications of* Bersch v. Drexel Firestone, Inc., *and* IIT v. Vencap, Ltd., 33 WASH. & LEE L. REV. 397 (1976); Note, *American Adjudication of Transnational Securities Fraud*, 89 HARV. L. REV. 553 (1976).

11. 540 F.2d 591 (3d Cir. 1976).

sufficient from a jurisdictional standpoint to apply the federal [securities] statutes. . . ."[12]

It could be argued that *Straub* differs somewhat from the case at hand. The stock in the *Straub* fraud was traded on an American OTC exchange, unlike the securities here which were not so traded. Frequently, trading on an exchange has helped to undergird findings of jurisdiction in other transnational fraud cases.[13] Where a stock exchange is involved, courts have found sufficient impact in the United States to sustain jurisdiction. In addition, there *may* have been slightly more conduct in the United States in *Straub* than in the present case, for Judge Weis said that the panel was "not here faced with a predominantly foreign transaction."[14] Despite these possible variations, however, *Straub* indicates that jurisdiction does exist in this case. This is so because Judge Weis flatly proclaimed that conduct in this country, standing alone, is enough for jurisdiction to attach under the federal securities laws.[15]

12. *Id.* at 595.

In so stating, Judge Weis referred to the Restatement (Second) of Foreign Relations Law of the United States §17(a) (1965):

> A state has jurisdiction to prescribe a rule of law (a) attaching legal consequences to conduct that occurs within its territory, whether or not such consequences are determined by effects of the conduct outside the territory. . . .

While §17 speaks to the permissible limits of an exercise of jurisdiction by this country, the *Straub* panel evidently concluded that Congress sought to employ its power to a considerable extent where securities transactions were concerned.

13. *See, e.g.*, Schoenbaum v. Firstbrook, 405 F.2d 200 (2d Cir. 1968); Kook v. Crang, 182 F. Supp. 388 (S.D.N.Y. 1960).

14. 540 F.2d at 595.

15. It should be noted that the district judge rendered both of his opinions before *Straub*, and so there may be some question whether he would have decided the present case as he did had he had the benefit of the subsequent opinion of this Court.

Perhaps the leading opinions which have delved into the problem of jurisdiction in transnational securities fraud cases are *IIT* v. *Vencap, Ltd.*[16] and *Bersch* v. *Drexel Firestone, Inc.*[17]—Second Circuit decisions written by Judge Friendly. Of these two cases, *IIT* is more supportive of subject-matter jurisdiction here. In *IIT*, the alleged securities fraud arose out of negotiations outside the United States. These negotiations led to the sale in the Bahamas of preferred stock in Vencap, a Bahamian corporation whose shares were not traded on any American exchange, to IIT, a Luxembourg investment trust. While the Second Circuit intimated that the defendants may well have engaged in sufficient conduct in this country to justify subject-matter jurisdiction under the Securities Acts,[18] the Court nonetheless remanded for additional findings as to the extent and nature of the intranational fraudulent activities. Even so, *IIT* is quite pertinent to the present appeal.

In suggesting that jurisdiction might exist in *IIT*, Judge Friendly made several asseverations which are very damaging to the position of defendants here. He expressly noted that there was "little factual support for the view that [defendants'] activities had a significant *effect* in the United States . . . ."[19] Despite the absence of impact within the United States, Judge Friendly declared that jurisdiction still could exist. In so doing, he essentially rejected the position taken by the defendants in the case before us, i.e., that substantial or even some impact in this country is a prerequisite to jurisdiction over extraterritorial securities transactions.

16. 519 F.2d 1001 (1975).

17. 519 F.2d 974 (1975).

18. The Court stated, for example that there was "an abundance of American activity . . . ." 519 F.2d at 1018.

19. *Id.* at 1016. (Emphasis added).

As critical as may be the rejection of an "effect" requirement is the following declaration in *IIT:*

> We do not think Congress intended to allow the United States to be used as a base for manufacturing fraudulent security devices for export, even when these are peddled only to foreigners. * * * it is hard to believe that Congress meant to prohibit the SEC from policing [such] activities within this country . . . .[20]

While the defendants here contend that this language constitutes dicta, it sets forth a sound proposition, and one which we now adopt.

In our view, the federal securities laws do grant jurisdiction in transnational securities cases where at least some activity designed to further a fraudulent scheme occurs within this country. There is nothing in §10(b) or its companion anti-fraud provisions to thwart their application to fraudulent transactions when the actual locus of the harm is outside the territorial limits of the United States. Indeed, by their own terms, the anti-fraud laws suggest that such application is proper. The securities acts expressly apply to "foreign commerce," thereby evincing a Congressional intent for a broad jurisdictional scope for the 1933 and 1934 Acts.[21] Moreover, §10(b) and its related provisions seem to be largely concerned with conduct, hav-

20. *Id.* at 1017.

21. We note, for example, the preambles to both Acts indicate that they are to apply to transactions in "interstate and foreign commerce. . . ." 48 Stat. 74 (1933); 48 Stat. 881 (1934). Similarly, the term "interstate commerce" is defined in both enactments as covering any trade, commerce, transportation and communication with "any foreign country." Section 2(7) of the Securities Act of 1933, 15 U.S.C. §77(b)(7); §3(a)(17) of the Securities Exchange Act of 1934, 15 N.S.C. §78c(a)(17). Unfortunately, the legislative history is silent respecting the jurisdictional scope questions at issue here.

ing no requirement that accomplishment of the attempted fraud be a precondition to statutory liability.[22]

We are, like the *IIT* court, skeptical that Congress wished to preclude all SEC suits for injunctive relief where the victim of a fraudulent scheme happens to be foreign or where there was insubstantial impact on the United States. Consequently, we decline to immunize, for strictly jurisdictional reasons, defendants who unleash from this country a pervasive scheme to defraud a foreign corporation. This would appear to be especially appropriate where the corporation is owned by a foreign governmental subdivision of a neighboring nation.

The *IIT* court did narrow its decision somewhat by saying: "Our ruling on this basis of jurisdiction is limited to the perpetration of fraudulent acts themselves and does not extend to mere preparatory activities or the failure to prevent fraudulent acts where the bulk of the activities were performed in foreign countries . . . ."[23]

In this case the defendants claim that their allegedly fraudulent conduct occurred primarily outside the United States. The district court embraced the defendants' contention in its original opinion, viewing the securities transactions as being "essentially foreign." Thereafter, in dismissing the amended complaint, the trial judge not

22. Rule 10b-5, 17 CFR 240.10b-5, for example, prohibits any person participating in securities transactions falling within interstate commerce, from "*employ*[*ing*] any device, scheme or artifice to defraud" or "*engag*[*ing*] *in any act,* practice or course of business which operates or *would* operate as a fraud. . . ." (emphasis added) Similar language also is present in §17(a) of the 1933 Act, 15 U.S.C. §77(g)(a) and in §10(b) of the 1934 Act, 15 U.S.C. §78(j)(b).

Also relevant here is SEC v. Capital Gains Research Bureau, 375 U.S. 180, 191-92 (1963), in which the Supreme Court held that the Commission need not prove that any investor has sustained loss as a result of a defendant's fraudulent activities in order to secure injunctive relief.

23. 519 F.2d at 1018.

only reaffirmed his initial position, but also sought to circumvent *IIT*, which had been decided shortly after the filing of the first opinion in this case. While the district court emphasized the above-quoted statement in *IIT*, which somewhat restricted the scope of that decision,[24] we do not believe that *IIT* may be disposed of by mere reference to such language. In our view, the conduct of the defendants here cannot be deemed to be "mere[ly] preparatory" to fraudulent acts committed outside this country, for it was much more substantial than the United States-based activities in *IIT*.[25] Consequently, it would appear that *IIT* supports jurisdiction over this SEC suit primarily for injunctive relief.[26]

Bersch v. *Drexel Firestone, Inc.*[27] is not quite as apposite as *IIT* to the case at bar, even though the *Bersch* court found jurisdiction in part. This is so since some of the *Bersch* victims were resident Americans, and therefore, unlike in *IIT* and our case, there was a definite impact on investors in this country. The Second Circuit did not, however, accord jurisdiction in *Bersch* over the claims of non-

24. *See* Opinion of District Court (unreported) at 3-4, Appendix at 267-68.

25. The findings of the district court on remand as to the nature and extent of the *IIT* defendants' conduct in this country as set forth at 411 F. Supp. 1094 (S.D.N.Y. 1975).

26. In his *IIT* opinion, Judge Friendly makes frequent reference to Leasco Data Processing Equipment Corp. v. Maxwell, 468 F.2d 1326 (2d Cir. 1972). In *Leasco*, an American corporation alleged that defendants had fraudulently induced it to purchase stock of a British corporation at exorbitant prices. The transaction occurred in England, and the stock was not registered nor traded in the United States. Nevertheless, the Second Circuit found subject-matter jurisdiction because the defendants had engaged in conduct in this country essential to furtherance of the fraud. It indicated that "significant" intranational conduct would be "sufficient" for subject-matter jurisdiction. *See* 468 F.2d at 1334.

27. 519 F.2d 974 (1975).

resident and foreign plaintiffs. Even so, *Bersch* does contain statements which buttress the result that we reach in this case.

Significantly, the *Bersch* court said that "the antifraud provisions of the federal securities laws . . . do not apply to loss from sales of securities to foreigners . . . unless acts . . . within the United States directly caused such losses."[28] Citing this statement, the defendants here claim that the losses of the Fund were not "directly caused" by acts within the territorial limits of this country. They postulate that conduct in *Bersch* similar to some of the conduct in our case, namely, meetings, drafting of agreements, bank transactions and mailings, was deemed insufficient to vest jurisdiction over the foreign plaintiffs in that situation.

Nevertheless, it appears that there was much more United States-based activity in the present case than in *Bersch,* including, *inter alia,* the execution of a key investment contract in New York as well as the maintenance of records in this country by both American and foreign corporations, records that were crucial to the consummation of the fraud. Not only do we believe that the sum total of the defendants' intranational actions was substantial, but we also question whether it can be convincingly maintained that such acts within the United States did not directly cause any extraterritorial losses. Rather, it is evident that the defendants' conduct occurring within the borders of this nation was essential to the plan to defraud the Fund. As a result, there is little in *Bersch* which stands against jurisdiction in the instant case, even in spite of the fact that the sole victim of the fraud was a Canadian corporation.

In sum, the prior pronouncements of this Court and those of the Second Circuit, a court with especial expertise

28. *Id.* at 993.

in matters pertaining to securities,[29] lend great support for a holding of jurisdiction here. *Straub, IIT* and, to a lesser extent, *Bersch* together indicate that such a ruling is the appropriate one. While those cases diverge somewhat from the factual setting present here, the differences do not, in our view, militate against reinstatement of the SEC's complaint seeking injunctive and ancillary relief.

III.

From a policy perspective, and it should be recognized that this case in a large measure calls for a policy decision,[30] we believe that there are sound rationales for asserting jurisdiction. First, to deny such jurisdiction may embolden those who wish to defraud foreign securities purchasers or sellers to use the United States as a base of operations. By sustaining the decision of the district court as to the lack of jurisdiction, we would, in effect, create a haven for such defrauders and manipulators. We are reluctant to conclude that Congress intended to allow the United States to become a "Barbary Coast," as it were, harboring international securities "pirates."

We also are concerned that a holding of no jurisdiction might induce reciprocal responses on the part of other nations. Some countries might decline to act against individuals and corporations seeking to transport securities frauds to the United States. Such parties may well be outside the ambit of the power of our courts. For foreign nations to adopt the position that the defendants are urging this Court to take would enable defrauders beyond the

29. *See* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 762 (1975) (Blackmun, J., dissenting). Blackmun referred to the Second Circuit as " 'the Mother Court' in [the securities] area of the law. . . ."

30. *See* Straub v. Vaisman & Co., 540 F.2d 591, 595 (3d Cir. 1976).

reach of our courts to escape with impunity. By finding jurisdiction here, we may encourage other nations to take appropriate steps against parties who seek to perpetrate frauds in the United States. Accordingly, our inclinations towards finding jurisdiction are bolstered by the prospect of reciprocal action against fraudulent schemes aimed at the United States from foreign sources.

As a final policy justification for asserting jurisdiction here, we register the opinion that the anti-fraud provisions of the 1933 and 1934 Acts were designed to insure high standards of conduct in securities transactions within this country in addition to protecting domestic markets and investors from the effects of fraud. By reviving the complaint in this case, this Court will enhance the ability of the SEC to police vigorously the conduct of securities dealings within the United States. Such a result would appear to comport with the basic purposes of the federal statutes.

IV.

It should be noted that reinstatement of the SEC's complaint does not dispose of the question of subject-matter jurisdiction once and for all. Rather, that issue may be raised again should the proofs at trial fail to correspond to or verify the factual allegations submitted by the SEC. If it should be disclosed that the allegedly fraudulent conduct of any of the defendants within this country was non-existent or was so minimal as to be immaterial, then the district court, or this Court on appeal, may be warranted in dismissing the action for want of jurisdiction.[31] As stated earlier, the decision we reach today rests upon the assumption that the facts tendered by the SEC are true.

The order of dismissal of the district court will be reversed and the matter remanded to that court for further proceedings consistent with this opinion.

31. *See* Leasco Data Processing Equipment Corp. v. Maxwell, 468 F.2d 1326, 1330 (1972).

APPENDIX B

Opinion of the District Court Dismissing Original Complaint, March 11, 1975

UNITED STATES DISTRICT COURT

DISTRICT OF NEW JERSEY

Civil Action No. 74-90

Securities and Exchange Commission,

Plaintiff,

v.

Alexander Kasser, Stephen E. Mochary, Technopulp Incorporated, Churchill Forest Industries (Manitoba) Ltd., Churchill Pulp Mill Ltd., James M. Brown, Jr., Chester Chastek, River Sawmills Company, and Blue Construction Corporation,

Defendants.

WHIPPLE, Chief Judge

The plaintiff Securities and Exchange Commission instituted this action for injunctive and other relief against nine individual and corporate defendants. As set forth in detail *infra,* the complaint alleges numerous violations of Section 17(a) of the Securities Act of 1933, 15 U.S.C. §77q (a), and Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), together with Rule 10b-5 thereunder, 17 CFR 240.10b-5. Additionally, there is a cross-claim in the cause which is not material at this stage of the proceedings.

With the exception of Alexander Kasser, who has yet to be served with process, all of the defendants have moved for dismissal of the complaint pursuant to Fed. R. Civ. P. 12(b)(1), asserting lack of subject matter jurisdiction. Should this Court deny those motions, defendants Brown, Chastek, River Sawmills Co. and Blue Construction Corporation have filed several alternative motions of which only the following are presently under consideration: (1) that the Manitoba Development Corporation (the allegedly defrauded Canadian entity) be joined as a party, or failing such joinder, that the action be dismissed for failure to join an indispensable party; and (2) that plaintiff's demand for an accounting and restitution by defendant Brown to the Manitoba Development Corporation be striken. Consideration of the remaining motions has been deferred pending disposition of the applications which are presently before the Court.

I. THE COMPLAINT

For the purposes of this motion, all well pleaded allegations of the complaint must be accepted as true. *Sabolsky* v. *Budzanoski*, 457 F.2d 1245, 1249 (3rd Cir.), *cert. denied*, 409 U.S. 853 (1972); *Lasher* v. *Shafer*, 460 F.2d 343, 344 (3rd Cir. 1972).

Count I of the complaint indicates that during the mid-1960's the Canadian provincial government of Manitoba sought to interest private enterprise in the creation of a forestry complex at The Pas, Manitoba. An organization called the Manitoba Development Fund (hereinafter M.D.F.), row known as the Manitoba Development Corporation, was created by the government to oversee the development and financing of the project. In 1965 Monoca, A.G., a Swiss corporation allegedly owned and controlled by defendant Alexander Kasser, a United States citizen, received an option to develop the complex. Oskar Reiser, a

Swiss national, negotiated the option on behalf of Monoca A.G. which, according to the complaint, purported to represent diverse European and American investors in the pulp and paper industry.

In January 1966, negotiations were held in New York, New York between Reiser and Manitoba officials concerning plans for the forestry project. On February 24, 1966 the Province of Manitoba signed an agreement in Canada with defendant Churchill Forest Industries (Manitoba), Ltd. (hereinafter C.F.I.). Under that contract C.F.I. was granted timber concessions in exchange for its commitment to develop, own, and operate the forestry complex. C.F.I. had been incorporated in Canada and was represented to be a subsidiary of Monoca. The defendant Kasser, however, allegedly concealed his complete ownership of both corporations.

The complaint asserts that in furtherance of the scheme defendant Kasser and others fraudulently induced the M.D.F. to enter an investment contract with C.F.I. That contract, entitled a Master Finance Agreement, was negotiated partially in New York but was executed in Canada on November 19, 1966. The agreement provided for the establishment of a forestry complex to be owned and operated by C.F.I. Financing for the project was to emanate principally from the M.D.F., but C.F.I. was required as a condition of the agreement to furnish substantial amounts of its own invested equity capital. The Master Finance Agreement defined said equity capital as money paid in cash for shares of C.F.I. stock, and expressly excluded the use of retained earnings and government grants under the so-called Canadian Area Development Incentives Act (hereinafter A.D.A.).

The very substance of the fraud upon which the complaint is based stems from alleged violations of this provision in the Master Finance Agreement. The defend-

ants, according to the complaint, used elaborate and complex methods of concealing the true nature of the purported equity capital investment in C.F.I.

By way of background, the complaint avers that Kasser's only role in the preliminary negotiations was that of president of the defendant Technopulp Incorporated (hereinafter Technopulp), a New Jersey corporation. When the Master Finance Agreement was signed, the M.D.F. approved a May 1966 engineering and management services contract signed by Kasser for Technopulp and Reiser for C.F.I., which was represented by defendants to be an arms-length transaction. Furthermore, the M.D.F. executed an agreement with Monoca A.G. in which Monoca represented that it would invest a minimum of $5,000,000 in C.F.I. stock by March 31, 1971. As in the Master Finance Agreement, the consideration for these shares was not to come from retained earnings of C.F.I. or from A.D.A. grants. Monoca claimed that it had a substantial interest in C.F.I. and that it would fully disclose any change in corporate ownership. Mr. Kasser was represented as having only a minor shareholder interest in Monoca. This so-called "Monoca Agreement", like the other contracts with the M.D.F., was not executed in the United States.

The complaint alleges further that, in employment of the scheme, defendants Kasser and Stephen Mochary, a New Jersey attorney, incorporated the defendant Churchill Pulp Mill, Ltd. (hereinafter Churchill Pulp) in Nevada during June 1969. On June 15, 1969 Technopulp and C.F.I. were consolidated in Churchill Pulp as wholly owned subsidiaries, a structural change which according to the allegations was never disclosed to the M.D.F. Through this device, it is asserted that the defendants were able to "channel" loan disbursements from the M.D.F. and earnings from the project into purported investments in C.F.I. stock.

It appears that Churchill Pulp, through an assignment to it by Kasser of his rights to C.F.I. stock, became responsible for investing the $5,000,000 in equity capital to which Monoca had agreed in the Monoca contract. This assignment was allegedly confirmed in a letter mailed by Mochary from Montclair, New Jersey to Kasser, whose address is not given. It is alleged that the M.D.F. was never informed of either assignment. As indicated *infra,* Churchill Pulp was eventually to hold the C.F.I. stock through its nominee, the Swiss Bank Corporation.

Paragraph 33 of the complaint contains allegations as to the "mechanics" of funneling M.D.F. money into C.F.I. stock in order to satisfy the requirements of the Master Financing Agreement. The defendants are claimed to have engaged in direct "recycling" of monies advanced as loans by the M.D.F. The scheme allegedly operated in the following manner: After having requisitioned certain monies from the M.D.F. to purportedly pay development costs, C.F.I. would deposit money in the Royal Bank of Canada at Winnipeg, Manitoba in an amount equal to the required percentage of equity investment for the requisition. When the Royal Bank confirmed that it received a deposit designated for stock purchases, the Canadian C.F.I. attorney would certify to the M.D.F. that such funds were received and would issue an appropriate amount of C.F.I. stock in the name of the Swiss Bank Corporation. The M.D.F. would then authorize disbursements of the loan requisition, and C.F.I. would complete the cycle by issuing debentures to the M.D.F. for the loan. While paragraph 33 does not *specifically* allege that the monies deposited in the Royal Bank were part of the same funds disbursed by the M.D.F., there are generalized allegations to that effect contained elsewhere in the complaint. It is thus assumed for the purpose of this motion that the same monies paid to C.F.I. in Canada were henceforth transferred to the Royal Bank as purported equity investments.

Another aspect of the scheme involved the New York office of the Swiss Bank Corporation into which defendants Kasser and Mochary allegedly channeled funds from the middle of June, 1969 until March of 1970. The Swiss Bank was instructed in letters from Mochary to transfer this money by wire from New York to the Royal Bank of Canada in Winnipeg, Manitoba, for the purchase of C.F.I. stock in the Swiss Bank's name. The Swiss Bank held this stock as nominee for Churchill Pulp, whose beneficial ownership was never disclosed to the M.D.F. The complaint asserts that over $3,000,000 in purported stock purchases were routed from Mochary's Montclair, New Jersey office to the New York conduit, and then by wire to the Royal Bank in Winnipeg. Approximately $1,700,000 of this sum was allegedly contributed by Technopulp in the form of dividends to its parent, Churchill Pulp.

The first count of the complaint indicates that a total of more than $38,000,000 was advanced by the M.D.F. to C.F.I. in the form of "loan disbursements and working capital loans". Defendants issued and delivered C.F.I. debentures to the M.D.F. in the total face amount of $40,700,000. In late 1970, C.F.I. defaulted on its interest payments and a receivership action was instituted in January, 1971. The M.D.F. was awarded all of its remaining assets by the Court of Queen's Bench in November, 1973.

Count II of the S.E.C.'s complaint alleges similar fraudulent acts on the part of the following defendants: Kasser, Mochary, James M. Brown, Jr., Chester Chastek, River Sawmills Company, a Delaware corporation (hereinafter River) and Blue Construction Corporation, a Delaware corporation (hereinafter Blue). The events contained in this Count occurred from January 1968 until January 16, 1974, the date of the complaint.

The details of the alleged fraud follow a pattern similar to the acts described in the first count. In early 1968, the

M.D.F. began to explore the economic feasibility of constructing a large sawmill at The Pas, Manitoba. For various reasons, the M.D.F. insisted on independent ownership of this project. In the summer of 1968, Kasser brought together the M.D.F. and defendant James M. Brown, Jr., who was chairman of a well-established, successful lumber operation called the Pack River Company which owned sawmills in the United States and Canada. Together with Kasser, Brown represented to the M.D.F. that he was willing to invest substantial sums of his own money and to assume the ownership and development of the sawmill.

In January, 1968, according to the complaint, defendants Kasser, Brown and Chester Chastek had met in Montclair, New Jersey to formulate a plan for developing the sawmill. Kasser and Brown agreed that the project would be a joint venture and that Kasser would lend Brown one-half of the front money to promote the operation. Furthermore, River would own the sawmill while Blue would construct a smaller mill for Churchill Pulp and would be the parent corporation for River.

In February, 1968, Kasser sent Brown a check for $25,000 to assist in the formation of Blue and was given the option to convert this loan into half the equity securities of Blue. During the same month, C.F.I. contracted with Blue in Montclair, New Jersey for the construction of a small sawmill at The Pas for the sum of $3,900,000. At a Sicily, Italy meeting in April, 1968, the defendants agreed to apply profits from the small sawmill toward equity in the larger project, with the balance of such equity to be provided through a Swiss bank loan. In late June, River entered into a construction contract with Blue for the large sawmill. The complaint does not specify where this contract was executed.

On September 25, 1968, in Montclair, New Jersey, Kasser, Brown and Chastek caused River to enter into a

Master Finance Agreement with the M.D.F. for development of the large sawmill project. As in its agreement with C.F.I., the M.D.F. promised to furnish the major portion of financing in installments which would be matched by proportionate contributions from River's equity. River also agreed to apply for an A.D.A. grant. Funds from this grant, as well as retained earnings, were expressly proscribed as contributions to River's equity capital. In negotiating with the M.D.F., the defendants represented that River was an affiliate of Brown's Pack River Company. To substantiate that representation, special stationery was allegedly printed in New Jersey for Pack River, denoting the defendant River as an affiliated company.

According to the complaint, the defendants fraudulently requisitioned from the M.D.F. $7,899,356 in four installments during the period from March 11, 1969 until March 26, 1970. Each time a disbursement was sought, the defendants are alleged to have created the false appearance that an additional increment in equity funds had been received by River. For example, the complaint asserts that on or about March 11, 1969, the defendant Chastek telephoned the M.D.F. from Spokane, Washington and falsely represented that River had received the $500,000 in stock purchases necessary under the Master Finance Agreement for requisition of funds. He later confirmed that representation by letter mailed from Spokane to Winnipeg. To substantiate the claim, $500,000 had been deposited in River's account with the Royal Bank Corporation loan and other money from Blue bank accounts in Seattle, Washington. Following the deposit by M.D.F. of $2,000,000 in River's Canadian account, Chastek directed the Royal Bank by telephone to transfer the funds to River's account at the Chemical Bank New York Trust Company in New York City. When the money was received by wire in

New York, Alexander Kasser's personal accountant directed that it be transferred from River's account to that of Blue Construction Corporation. Blue thereupon repaid the Swiss Bank loan which originated the transaction.

Similar requisitions were allegedly obtained in August and October, 1969, and in March of 1970. On two occasions, the initial $500,000 placed in River's account was obtained from the account of Blue at the Swiss Bank's New York office. The source of Blue's funds is alleged to have been a previous M.D.F. advance. With respect to the August disbursement, the source of that initial sum was a loan from Technopulp Machinery, Inc., a New Jersey corporation controlled by Alexander Kasser. The complaint alleges that in each transaction, the M.D.F. funds eventually ended up in Blue's New York account.

Pursuant to this scheme, the defendants issued and delivered to the M.D.F. debentures of River with a face amount of approximately $9,600,000. The equity securities allegedly issued by River were valued at approximately $9,600,000.

When the defendants sought another requisition in April, 1970, the M.D.F. refused to release the monies until River had accounted for the loans already received. Although defendants assertedly attempted to create a false appearance of equity investment similar to those described above, the funds were never released. The River operation was shut down in June, 1970. Because River defaulted on its interest payments to the M.D.F. later that year, a receivership action was instituted in the Court of Queen's Bench in January, 1971. M.D.F. was awarded all of River's remaining assets by that court in November, 1973. It is alleged that the simultaneous defaults of River and C.F.I. were in furtherance of the scheme designed by the defendants.

II. SUBJECT MATTER JURISDICTION

This Court's determination of the various motions to dismiss is dependent upon the resolution of a singular yet delicate issue: whether Congress, in enacting the securities legislation, intended to confer upon the federal courts jurisdiction to entertain actions involving the particular facts alleged in the Commission's complaint.

The basic thrust of defendants' argument is that the transactions alleged in the complaint were essentially foreign in nature having no significant impact on either the domestic investing public or the domestic securities markets. Absent the existence of such impact, it is urged that this Court is deprived of subject matter jurisdiction notwithstanding the various allegations of miscellaneous activities occurring within the United States. Conceding that there has been no direct impact,[1] the Commission nevertheless asserts that the federal courts are vested with jurisdiction where a scheme to defraud foreign entities is devised in this country by Americans who utilize the means of interstate commerce to achieve their objectives. For the reasons hereinafter stated, it is concluded that the complaint fails to invoke the subject matter jurisdiction of this Court; therefore, the defendants' motions to dismiss will be granted.

At the heart of the jurisdictional issue is of course the language of the statutes under which this action was instituted. Section 17(a) of the Securities Act of 1933 (hereinafter Securities Act) provides:

> (a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in inter-

1. During oral argument on the motions, Mr. Sullivan, counsel for the Commission, acknowledged "Again, I will say that as far [as] direct impact on our securities markets are concerned, there is no direct impact."

> state commerce or by the use of the mails, directly or indirectly—
>
> (1) to employ any device, scheme or artifice to defraud, or
>
> (2) to obtain money or property by means of any untrue statement of a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 10(b) of the Securities Exchange Act of 1934 (hereinafter Exchange Act), also cited in the complaint, contains a similar provision making it unlawful for any person

> by the use of any means or instrumentality of interstate commerce . . .
>
> (b) to use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.[2]

In support of its position, the Commission emphasizes the words "any person" and "any securities" in those

2. Since the statute is not self-executing, Rule 10b-5 was promulgated by the Commission. Jurisdiction, however, is unaffected by the language of that Rule.

statutes, the reference to "foreign commerce"[3] in the preambles to each, and the definition of interstate commerce in each as including trade, commerce, transportation, or communication "between any foreign country and any State." Securities Act §2(7); Exchange Act §3(a)(17). On the surface, the cited language reveals *only* that, when measured against the facts in this case, Congress did not prescribe an immediate jurisdictional solution to this problem of transnational law. As the Court of Appeals for the Second Circuit observed in the noted case of *Leasco Data Processing Equipment Corp.* v. *Maxwell,* 468 F.2d 1326, 1334 (2nd Cir. 1972):

> [T]he language of §10(b) of the Securities Exchange Act is much too inconclusive to lead us to believe that Congress meant to impose rules governing conduct throughout the world in every instance where an American company bought or sold a security.

At this juncture, it should be noted parenthetically that the vast majority of decisions in which similar jurisdictional issues have arisen, many of which are cited *infra,* involved section 10(b) of the Exchange Act and Rule 10b-5. The jurisdictional principles applicable to those provisions are identical to the principles which relate to section 17(a) of the Securities Act; hence any reference herein to one statute shall be deemed applicable to the other.

As early as 1909, the United States Supreme Court announced a presumption against the extraterritorial application of federal legislation. In *American Banana Co.* v. *United Fruit Co.,* 213 U.S. 347 (1909), the Court found that the Sherman Antitrust Act could not be applied to

3. For example, the preamble to the Securities Act states that the Act is intended to "provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof and for other purposes."

an action between two American corporations in which the plaintiff did not allege that defendants' activities had a substantial effect within the United States. In *United States* v. *Aluminum Co. of America,* 148 F.2d 416 (2d Cir. 1945), Judge Learned Hand reiterated that

> [w]e should not impute to Congress an intent to punish all whom its courts can catch, for conduct which has no consequences within the United States.

148 F.2d at 443. *See also Blackmer* v. *United States,* 248 U.S. 421, 437 (1937); *Restatement (Second) of the Foreign Relations Law of the United States* §38 (1965). In the realm of economic regulation, where Congress is primarily concerned with domestic affairs, the presumption against extraterritorial application is particularly strong. *See Foley Bros., Inc.* v. *Filardo,* 336 U.S. 281, 285 (1949). It is now abundantly clear, however, that the presumption may be rebutted so as to permit the assumption of jurisdiction where there are allegations that the extraterritorial conduct produced domestic impact which is violative of federal law. *United States* v. *Aluminum Co. of America, supra; Strassheim* v. *Daily,* 221 U.S. 280, 285 (1911).[4]

4. This is the so-called "objective" territorial principle of jurisdiction found in international law. As commonly construed, the objective principle requires that defendants' conduct was both intended to and did produce effects within the forum state. It is reflected in the *Restatement (Second) of Foreign Relations Law* at §18. The various principles have been widely discussed in the context of securities regulation and need not be dealt with here. *See, e.g.* Note, 7 Vand. J. Trans. L. 770 (1974); Note, 8 Tex. Intl. L.J. 430 (1973); Note, 10 Colum. J. Trans. L. 150 (1971); and the multitude of citations therein. Noteworthy is the observation frequently made that the presumption having caused "harsh" results in earlier cases, has been weakened by subsequent decisions such as *Alcoa.* As the analysis contained *infra* discloses, the Court agrees that jurisdiction has been expanded to include a variety of situations, but the presumption nevertheless survives. *See Leasco Data Processing Equipment Corp.* v. *Maxwell,* 468 F.2d 1326 (2d Cir. 1972); *Vanity Fair Mills Inc.* v. *T. Eaton Co.,* 234 F.2d 633 (2d Cir.) *cert. denied,* 352 U.S. 871 (1956).

The Commission urges this Court to utilize the jurisdictional principle embodied in the *Restatement (Second) of Foreign Relations Law of the United States* §17(a) (1965):

> A state has jurisdiction to prescribe a rule of law (a) attaching legal consequences to conduct that occurs within its territory, whether or not such consequences are determined by the effects of the conduct outside the territory . . .[5]

The Court agrees that on its face the *Restatement* approach would appear to permit the exercise of jurisdiction where, as here, conduct has occurred within United States borders. As defendants assert, however, it is essential to distinguish between the permissible limits of jurisdictional power recognized by international law and the extent to which Congress has chosen to implement that power. In short, the question of extraterritorial application in this case is one of municipal, rather than international law. *United States* v. *Aluminum Co. of America, supra* at 148 F.2d 443. In *Leasco Data Processing Equipment Corp.* v. *Maxwell, supra,* the Court considered the *Restatement* in depth and observed:

> Conduct within the territory alone would seem sufficient from the standpoint of jurisdiction to prescribe a rule. It follows that when, as here, there has been significant conduct within the territory, a statute cannot properly be held inapplicable simply on the ground that, absent the clearest language, Congress will not be assumed to have meant to go beyond the limits recognized by foreign relations law. . . .
>
> . . . .

5. This section states the "subjective" territorial principle of jurisdiction. *See, e.g.* Note, 69 Colum. L. Rev. 94 (1969) and citation therein.

> Up to this point we have established only that, because of the extensive acts alleged to have been performed in the United States, considerations of foreign relations law do not preclude our reading §10(b) as applicable here. The question remains whether we should.

468 F.2d at 1334-35.

With this background in mind, it is essential to juxtapose the underlying purposes of the securities fraud legislation in order to place the facts of this case in their proper perspective. It is beyond dispute that the principal objective is protection of *American* purchasers who are exposed to fraudulent offers or sales of securities in interstate commerce.

In *Shoenbaum* v. *Firstbrook,* 405 F.2d 200 (2d Cir. 1968), the Second Circuit considered this objective in terms of its transnational application:

> We believe that Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities on American Exchanges[6] and to protect the domestic securities market from the effects of improper foreign transactions in American securities.

405 F.2d at 206.

The latter part of that statement is reflective of defendants' position in the instant case: Congress did not intend to confer jurisdiction on the federal courts over an essentially foreign transaction in American securities *unless* that transaction has an impact on domestic investors or securities markets. This Court agrees with that contention.

6. In *Leasco, supra,* the Court reviewed the statute and legislative history and concluded that the protection is not limited to the organized markets. In light of that extensive review, this Court need not reexamine the legislative history.

Curiously, both plaintiff and defendants rely on many of the same authorities to support their respective claims. The Commission asserts that applicable precedent requires only that there be a use of the jurisdictional means in connection with fraudulent conduct, regardless of the non-existence of impact or effects in this country. As defendants suggest, a careful review of comparable decisions in which jurisdiction has been sustained discloses a requisite effect or impact upon American investors or securities markets *in addition to* the use of interstate commerce facilities by the defendants. Hence these cases are clearly distinguishable since there is concededly no impact in the case at bar. *See e.g., Securities and Exchange Commission* v. *United Financial Group, Inc.*, 474 F.2d 354 (9th Cir. 1973); *Shoenbaum* v. *Firstbrook*, 405 F.2d 200 (2d Cir. 1968), *rev'd in part on other grounds en banc*, 405 F.2d 215, *cert. denied*, 395 U.S. 906 (1969).

In *Leasco Data Processing Corp.* v. *Maxwell, supra*, upon which all of the parties heavily rely, the court clarified its view thusly:

> [W]e doubt that impact on an American company and its shareholders would suffice to make the statute applicable if the misconduct had occurred solely in England, we think it tips the scales in favor of applicability when substantial misrepresentations were made in the United States.

468 F.2d at 1337. *See also Travis* v. *Anthes Imperial Ltd.*, 473 F.2d 515, 526 n.21 (8th Cir. 1973), in which Canadian defendants had defrauded American shareholders of a Canadian corporation:

> [T]he transaction involved is one which to a significant degree has taken place within the United States, has caused injury to United States investors, and the jurisdiction is grounded on more than an incidential use of the mails or the facilities of interstate commerce.

Cf. *Roth* v. *Fund of Funds, Ltd.*, 405 F.2d 421 (2d Cir. 1968), *cert. denied*, 394 U.S. 975 (1969). Although the Commission vigorously urges that it is controlling, *Securities and Exchange Commission* v. *Gulf Intercontinental Finance Corp.*, 223 F. Supp. 987 (S.D. Fla. 1963) is likewise distinguishable. The Court there found that, while no Americans had purchased stock as a result of the allegedly fraudulent offers, American investors had undoubtedly been exposed to the offers on a wide scale. Jurisdiction was thus proper since the Court found that the securities laws clearly apply to the offer of foreign securities within the United States. The complaint in this case is utterly devoid of similar allegations.

Defendants have alluded to the following persuasive language in *Investment Properties International, Ltd.* v. *I.O.S., Ltd.*, CCH Fed. Sec. L. Rep. ¶93,011 at 90,727 (S.D. N.Y. 1971) *aff'd mem*, Docket No. 71,572 (2d Cir. 1971):

> [A]lthough the behavior of a defendant, including its connection to the United States and to the domestic securities market and exchanges, is relevant in deciding whether an extraterritorial transaction comes within the jurisdiction of the Act, the main consideration appears to be: Does the transaction have some significant impact on the domestic securities market or on domestic investors, and is extraterritorial application therefore necessary to protect securities trading in the United States and/or American investors?

It is of course clear in the case *sub judice* that there is no showing of domestic impact caused by the allegedly fraudulent conduct of the defendants. On this basis alone, it cannot fairly be said that Congress intended to reach these transactions in the anti-fraud legislation. The Court's in-

quiry, however, must go one step further in order to determine whether the activities conducted by the American defendants in the United States, though concededly without effect here, were sufficient to give rise to jurisdiction.

In the opinion of this Court, the essentially foreign nature of the transaction here at issue is not materially altered by the various miscellaneous acts allegedly committed locally in furtherance of the scheme. To reiterate, those activities include the following: (1) meetings were held in the United States as part of negotiations; (2) a New York office of the Swiss Bank Corporation was used as a conduit for the transfer of funds, although only a relatively small portion of those funds was actually so transferred through that bank; (3) one Master Finance Agreement was executed in New York; (4) defendants incorporated most of the corporations in this country and discussed their plans in New Jersey; and, (5) the means of interstate commerce (mails, telephone and telegraph) were employed in furtherance of the scheme. While these domestic activities, in particular the use of American corporations, cannot be ignored, the Court is nonetheless satisfied that the case before it involves essentially foreign transactions without impact in this country.

A single Canadian entity has invested in debt securities of closely held corporations. The securities were never traded in or even exposed to American markets or investors. Moreover, the securities were given in exchange for funds to be used exclusively in the development of a Canadian forestry complex. The principal issuer of those securities was a Canadian corporation which allegedly transferred the M.D.F. money directly to a Canadian bank, without the use of American conduits. All but one of the contracts involved were executed outside the country. The existence of American defendants notwithstanding, this Court concludes that it was not the intent of Congress to

include essentially foreign transactions such as these within the ambit of the federal anti-fraud legislation. See *Investment Properties International, Ltd.* v. *I.O.S., supra; Manus* v. *Bank of Bermuda, Ltd.*, CCH Fed. Sec. L. Rep. ¶93,299 (S.D.N.Y. 1971); *Finch* v. *Marathon Securities Corp.*, 316 F. Supp. 1345 (S.D.N.Y. 1970); *Sinva, Inc.* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 48 F.R.D. 385 (S.D.N.Y. 1969); *Kook* v. *Crang*, 182 F. Supp. 388 (S.D.N.Y. 1960).

In conclusion, it should be noted that the Court recognizes the seriousness of the allegations against these defendants and the potential ramifications of this decision. Furthermore, it is entirely possible that there exists a legitimate governmental interest in applying the securities legislation to Americans who fraudulently issue securities in essentially foreign transactions. However, the Court remains convinced that this is not the proper forum for adjudication of the controversy. Accordingly, the motions to dismiss will be granted.

III. REMAINING MOTIONS

In light of the Court's disposition of the jurisdictional motions, it is of course unnecessary to consider any of the remaining motions in the cause.

Defendants shall submit an appropriate order.

No Costs.

/s/ Lawrence A. Whipple

Lawrence A. Whipple
Chief Judge, U.S.D.C.

Dated: March 11, 1975

APPENDIX C

Opinion of the District Court Dismissing Amended Complaint, November 17, 1975

UNITED STATES DISTRICT COURT

DISTRICT OF NEW JERSEY

Civil Action No. 74-90

Securities and Exchange Commission,

Plaintiff,

v.

Alexander Kasser, Stephen E. Mochary, Technopulp Incorporated, Churchill Forest Industries (Manitoba) Ltd., Churchill Pulp Mill Ltd., James M. Brown, Jr., Chester Chastek, River Sawmills Company, and Blue Construction Corporation,

Defendants.

WHIPPLE, Chief Judge

This case is before the Court on defendants' motions to dismiss the plaintiff Securities and Exchange Commission's amended complaint. The facts are set forth in the Court's opinion in *Securities and Exchange Commission* v. *Kasser,* 391 F. Supp. 1167 (D.N.J. 1975). Having reviewed the amended complaint, this Court finds that said complaint contains no new allegations of domestic impact and merely restates in more lengthy fashion the substance of the SEC's initial complaint.

Appendix C

In opposing defendants' motions to dismiss, the SEC merely restates its position that this Court has subject matter jurisdiction of an action by the SEC where the defendants' allegedly used the United States as a base to defraud foreign investors even in the absence of direct impact on domestic investors or the domestic securities markets. In effect, the SEC seeks to have this Court reconsider its opinion of March 11, 1975, granting defendants' motions to dismiss the SEC's initial complaint. In support of its position, the SEC relies on the Second Circuit's recent decision in *IIT* v. *Vencap, Ltd.,* 519 F.2d 101 (2d Cir. 1975). A review of that case and its companion case, *Bersch* v. *Drexel Firestone, Inc.,* 519 F.2d 974 (2d Cir. 1975), however, demonstrates that the Second Circuit's recent development of the law is not inconsistent with this Court's opinion of March 11, 1975.

In *IIT,* the defendant Pistell was a United States citizen living in the Bahamas. He formed Vencap, Ltd., as a Bahamian corporation to engage in the venture capital business. He and an associate purchased control in Vencap for about $1,000.00. Pistell then persuaded an executive of the Investors Overseas Services, Ltd., (IOS) mutual fund complex to invest about $30,000.00 of IIT (an IOS subsidiary) funds in preferred stock of Vencap. There was some evidence that the stock subscription agreement had been drafted in New York. Following the sale of the stock by Vencap, Pistell allegedly siphoned money from Vencap through fraudulent schemes. The schemes allegedly involved transactions in New York.

On appeal, the Second Circuit first found that there had been no "substantial effect" upon United States investors or securities markets for purposes of subject matter jurisdiction. 519 F.2d at 1016-17. However, the Court stated that the absence of such effect did not necessarily defeat jurisdiction, where the fraudulent activity complained of

was conducted in the United States. 519 F.2d at 1017. But the Court was very careful to limit its holding, stating:

> Our ruling on the basis of jurisdiction is *limited to the perpetration of fraudulent acts themselves and does not extend to mere preparatory activities . . . where the bulk of the activity was performed in foreign countries.* . . . Admittedly, this distinction is a fine one. But . . . the line has to be drawn somewhere if the securities laws are not to apply in every instance where something has happened in the United States, *however large the gap between the something and a consummated fraud and however negligible the effect in the United States or on its citizens.*

519 F.2d at 1018 (emphasis added).

Admittedly, the *IIT* holding "goes beyond any case yet decided." *Bersch, supra,* 519 F.2d at 987. However, even given the extension, *IIT* does not require a different decision in this case. The Second Circuit carefully pointed out in its opinion that it would uphold jurisdiction only if the fraudulent acts were performed in the United States. [The Court was unable to issue a definitive holding because the record was unclear as to exactly what fraudulent acts had been committed in New York]. In *Kasser,* however, the alleged fraud was consummated in Canada where the Manitoba Development Fund (MDF) transferred funds to defendants in exchange for debentures. The activities conducted in the United States were more in the nature of preparatory activities than was the case in *IIT. Kasser* involves a situation where the gap is large "between the [local acts] and a consummated fraud," and where the "effect in the United States or on its citizens" is miniscule. *IIT, supra,* 519 F.2d at 1018.

An examination of this Court's ruling in *Kasser* in light of *IIT* would be incomplete without consideration of the companion case to *IIT, Bersch* v. *Drexel Firestone, Inc.,*

519 F.2d 974 (2d Cir. 1975). In *Bersch,* IOS, Ltd., an entity primarily engaged in the sale and management of mutual funds, entered into a scheme whereby each of IOS's subsidiaries would go public. The prospectus specified that the offering was made only to employees and others having an interest in IOS and further stated that the offering was not to be made in the United States. Subsequently, the price of shares plummeted to nearly zero, and the holders of the stock (all foreign citizens) brought suit under the Securities Act.

The trial judge found that there had been extensive activities within the United States, including, *inter alia,* 1) representatives of IOS, its underwriters, attorneys and accountants met in New York on numerous occasions to initiate, organize and structure the offering; 2) parts of the prospectus were drafted in New York; 3) accounts for the proceeds of the underwriting were opened in New York. 519 F.2d at 985 n.24. On appeal the Second Circuit ruled that such activities did not suffice to confer subject matter jurisdiction. The Court regarded the fraud as having occurred when the allegedly false and misleading prospectuses were issued. The prospectuses were in all instances issued in foreign cities, *e.g.,* London, Brussels, Toronto, hence the fraud was essentially foreign in nature. The Court stated:

> [W]e see no reason to extend [the *IIT* holding] to cases where the United States activities are merely preparatory . . . *and are relatively small in comparison to those abroad.*

519 F.2d at 987 (emphasis added). In further explicating its holding, the Court hypothesized a situation strikingly similar to that in *Kasser.* The Court stated:

> Assuming that there were no American purchasers and that the underwriting related, for example, to a

> large [foreign industrial company clearly identified with a] foreign country rather than with the United States . . . we do not believe the activities in the United States . . . would justify an American court in taking jurisdiction in a suit for damages by foreign plaintiffs.

519 F.2d at 986-987. In *Kasser,* there were no American citizens defrauded and the fraud related to a large foreign entity (MDF) clearly identified with Canada rather than with the United States. In this situation *Bersch* suggests jurisdiction is inappropriate.

This Court's reading of *IIT* and *Bersch* is supported by the recent decision in *F.O.F. Proprietary Funds, Ltd.* v. *Arthur Young & Co., et al.* Civ. No. 73-3282 (S.D.N.Y., September 24, 1975). In *F.O.F.* Judge Bonsal dismissed for lack of subject matter jurisdiction a complaint charging securities acts violation, where many acts were alleged to have occurred in the United States. The acts alleged included: 1) the securities that were the subject of the alleged fraud were debentures of a United States corporation; 2) the misleading offering circular was drafted and reviewed by the defendants in New York; 3) the sale of the securities was authorized in the United States; 4) decisions as to the use of the proceeds of the alleged fraud were made in the United States; and 5) certain sales activities occurred in the United States. The Court concluded that under the *IIT/Bersch* analysis subject matter jurisdiction did not exist because the alleged fraudulent transaction was "predominantly foreign." Slip Opinion at 8. The Court characterized the activity in the United States as merely preparatory to the actual fraud, which involved the *acquisition abroad* by a *foreign corporation* of stock in reliance on offering certificates *distributed abroad,* resulting in the plaintiff incurring losses *abroad. Id.* at 8-9. As in *F.O.F.,* the alleged fraud in *Kasser* involved misrepresentations made abroad to a foreign corporation, resulting in the defrauded entity incurring losses abroad.

This Court concludes that plaintiff SEC's amended complaint construed in light of the Second Circuit's recent decisions in *IIT* and *Bersch* is insufficient to confer subject matter jurisdiction over this suit. Accordingly, defendants' motions to dismiss the amended complaint will be granted. No costs to any of the parties.

Defendants shall submit an appropriate order.

/s/ LAWRENCE A. WHIPPLE

LAWRENCE A. WHIPPLE
Chief Judge, U.S.D.C.

Dated: November 17, 1975.

APPENDIX D

Statutes and Regulations Involved

Sections 17(a), 20(b) and 22 of the Securities Act of 1933, 15 U.S.C. §§77q(a), 77t(b) and 77(v), provide as follows:

Section 17. (a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 20. (b) Whenever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this title, or of any rule or regulation prescribed under authority thereof, it may in its discretion, bring an action in any district court of the United States, United States court of any Territory, or the district court of the United States for the District of Columbia to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond. The Commission

may transmit such evidence as may be available concerning such acts or practices to the Attorney General who may, in his discretion, institute the necessary criminal proceedings under this title. Any such criminal proceeding may be brought either in the district wherein the transmittal of the prospectus or security complained of begins, or in the district wherein such prospectus or security is received.

Section 22. (a) The district courts of the United States, the United States courts of any Territory, and the district court of the United States for the District of Columbia shall have jurisdiction of offenses and violations under this title and under the rules and regulations promulgated by the Commission in respect thereto, and, concurrent with State and Territorial courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this title. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the offer or sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 225 and 347.) No case arising under this title and brought in any State court of competent jurisdiction shall be removed to any court of the United States. No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts.

(b) In case of contumacy or refusal to obey a subpena issued to any person, any of the said United States courts within the jurisdiction of which said person guilty of contumacy or refusal to obey is found or resides, upon application by the Commission may issue to such person an order

requiring such person to appear before the Commission, or one of its examiners designated by it, there to produce documentary evidence if so ordered, or there to give evidence touching the matter in question; and any failure to obey such order of the court may be punished by said court as a contempt thereof.

Sections 10(b), 21(e) and (f), and 27 of the Securities Exchange Act of 1934, 15 U.S.C. §§78j(b), 78u(e) and (f), and 78aa, provide as follows:

Section 10. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Section 21. (e) Upon application of the Commission the district courts of the United States, the United States District Court for the District of Columbia, and the United States courts of any territory or other place subject to the jurisdiction of the United States shall also have jurisdiction to issue writs of mandamus, injunctions, and orders commanding (1) any person to comply with the provisions of this title, the rules, regulations, and orders thereunder, the rules of a national securities exchange or registered securities association of which such person is a member or person associated with a member, the rules of a registered clearing agency in which such person is a participant, and the rules

of the Municipal Securities Rulemaking Board, or any undertaking contained in a registration statement as provided in subsection (d) of section 15 of this title, (2) any national securities exchange or registered securities association to enforce compliance by its members and persons associated with its members with the provision of this title, the rules, regulations, and orders thereunder, and the rules of such exchange or association, or (3) any registered clearing agency to enforce compliance by its participants with the provisions of the rules of such clearing agency.

(f) Notwithstanding any other provision of this title, the Commission shall not bring any action pursuant to subsection (d) or (e) of this section against any person for violation of, or to command compliance with, the rules of a self-regulatory organization unless it appears to the Commission that (1) such self-regulatory organization is unable or unwilling to take appropriate action against such person in the public interest and for the protection of investors, or (2) such action is otherwise necessary or appropriate in the public interest or for the protection of investors.

Section 27. The district courts of the United States, the district court of the United States for the District of Columbia, and the United States courts of any Territory or other place subject to the jurisdiction of the United States shall have exclusive jurisdiction of violations of this title or the rules and regulations thereunder, and of all suits in equity and actions at law brought to enforce any liability or duty created by this title or the rules and regulations thereunder. Any criminal proceeding may be brought in the district wherein any act or transaction constituting the violation occurred. Any suit or action to enforce any liability or duty created by this title or rules and regulations thereunder, or to enjoin any violation of such title or rules and regulations, may be brought in any such district or in the district wherein the defendant is found or is an

inhabitant or transacts business, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 128 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 225 and 347). No costs shall be assessed for or against the Commission in any proceeding under this title brought by or against it in the Supreme Court or such other courts.

Securities and Exchange Commission Rule 10b-5, 17 C.F.R. 240.10b-5, provides as follows:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(a) to employ any device, scheme, or artifice to defraud,

(b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.